Commodity Spotlight

Prices for Bumper Soybean Crop Hinge on China's Imports

Early this year, very dry conditions that began in the summer of 1999 prevailed over much of the nation's major soybean producing region. Soybean prices rallied in response to expectations of lower production in 2000. In late April and early May, dry soils allowed a rapid planting pace for spring crops, and partly in response to the price rise, U.S. farmers planted 74.5 million acres of soybeans for 2000, a 1-percent rise from last year's record. Nearly all of this year's increase was in the Northern Plains and Lake States, where crop rotations are still adjusting to incorporate more soybeans.

Following planting, abundant summer rains fell (though not in the Southeast), greatly increasing soil moisture. Once the threat of widespread drought disappeared, soybean prices fell sharply in anticipation of large production. Based on the record acreage and a national average yield forecast of 40.7 bushels per acre, USDA forecasts a record U.S. soybean crop in 2000 of 2.99 billion bushels. This year's output will likely exceed the 1998 record by nearly 250 million bushels. With beginning stocks large, U.S. soybean supplies are expected to rise 9 percent.

Despite this liberal supply expansion, U.S. soybean exports in 2000/01 are projected to rise only slightly, to 1,010 million bushels from last season's record 975 million. Primary reasons for the modest export growth are larger soybean harvests in China and South America and shrinking imports by the European Union (EU). In addition, the strength of the U.S. dollar compared with currencies of major export competitors and import buyers continues to curtail U.S. foreign trade.

With U.S. soybean demand expected to lag supply growth, ending stocks in 2000/01 are projected to swell to 465 million bushels from 280 million in 1999/2000, keeping downward pressure on soybean and soybean product prices. The 2000/01 soybean farm price is expected to average $3.90–$4.80 per bushel, down from the 1999/2000 average of $4.65, and to remain well below the loan rate ($5.26 per bushel) for the third consecutive year. Thus, loan benefits will continue to be important for soybean producers. Large supplies of corn and other feeds will also put downward pressure on soybean prices.

World oilseed production in 2000/01 is anticipated up 3.3 percent to 308 million metric tons. Virtually all of the increase is due to an 8-percent rise in expected soybean production. The U.S. and China account for three-fourths of the forecasted soybean output gain, with comparatively modest changes for most other countries. Growth in output by China, a major importer, is expected to contribute significantly to a projected fall in global soybean exports, from 46.3 million tons in 1999/2000 to 45.6 million.

China & European Union To Curb Imports

China's domestic prices for soybeans and products, unlike those of most nations, remain firm due to strong domestic demand and restrictive import policies. Vegetable oil prices within China, for example, are typically more than double world prices, because strict import quotas on vegetable oils maintain this price wedge. For oilseeds, however, a relative absence of import barriers provides a substantial advantage to domestic crushers in producing the highly valued vegetable oil. With recent changes in China's import policies for the soybean complex, including the re-imposition of a value-added tax on soybean meal in 1998 (*AO* September 1999), the country has successfully shifted toward greater reliance on domestic oilseed-crushing capacity vs. imports of protein meal and vegetable oil.

China's soybean imports soared 31 percent in 1998/99 and more than doubled to a record 9 million tons in 1999/2000, accounting for nearly 80 percent of world expansion in soybean trade last season. Soybean exports from the U.S. to China nearly tripled in 1999/2000, up from 9 percent of total U.S. exports to 17 percent. Conversely, China's imports of soybean meal and soybean oil plunged in 1999/2000 from 2 years earlier. U.S. shipments of soybean meal and soybean oil to China in 1999/2000 fell 100 percent and 80 percent, respectively.

Factors that drove the surge in China's 1999/2000 soybean imports also encouraged its own farmers to sow more soybeans this year instead of corn. China's soybean area in 2000 is estimated up 10 percent, which would push the projected crop to a relatively large 15 million tons (a serious drought is expected to reduce yields in northeastern China). As a result, China's soybean imports are expected to fall by one-fifth to 7.25 million tons in

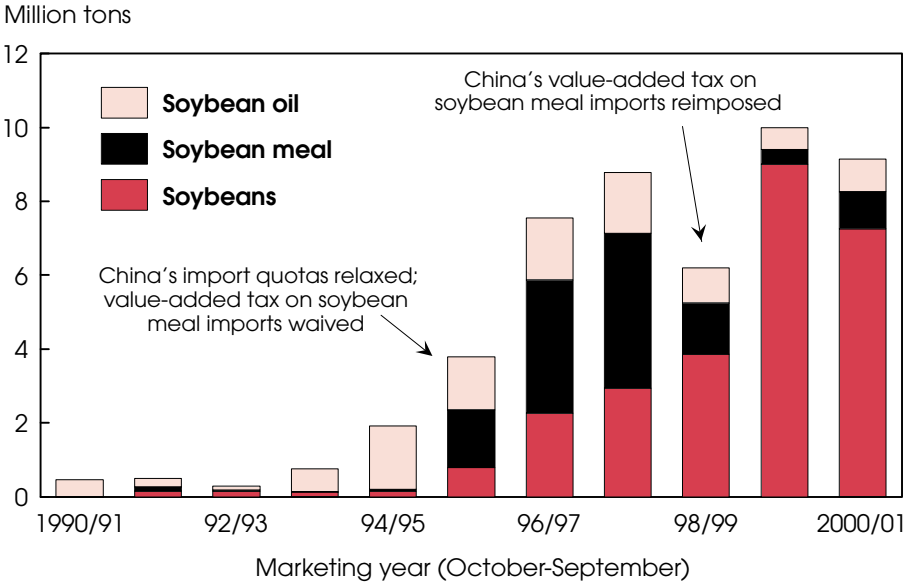
2000/01. The much larger domestic oilseed harvest would also mean that growth in Chinese imports of protein meal and vegetable oil will be modest next year, even if import barriers are lowered.

European Union soybean imports also are expected to decline in 2000/01, despite smaller domestic oilseed harvests and greater availability of global soybean supplies. The EU's recently implemented reforms (Agenda 2000) of the Common Agricultural Policy will allow minimum internal grain prices to fall 15 percent over the next 2 years. Since WTO commitments cap subsidized EU grain exports, much of the surplus will be fed to domestic livestock, thereby reducing EU soybean meal consumption. The substitution of grains will depress soybean meal prices and EU crushing margins. USDA projects EU soybean meal consumption to decline to 27.1 million tons in 2000/01 from 27.7 million in 1999/2000. The reduction is expected to trim EU imports of soybeans and soybean meal from 16.8 million to 16.3 million tons and from 20 million to 19.6 million tons, respectively.

In **India**, large vegetable oil imports weakened demand for domestic oilseeds earlier this year, keeping farm prices for soybeans just above the government support level and curbing area planted. However, normal development of India's monsoon is helping soybean yields recover from excessive dryness last year, and India's 2000/01soybean harvest is estimated up 10 percent to 5.7 million tons. India does not export soybeans but processes the entire crop for the soybean oil, exporting the surplus soybean meal produced. A larger soybean crop would boost projected Indian soybean meal exports to 2.5 million tons from 2.3 million in 1999/2000.

Late this year, as **South American** soybean farmers make planting decisions, greater U.S. and Indian competition and slower imports by China, the EU, and Japan will dim their price outlook. As in 1999/2000, the expansion in *Brazilian* soybean area should remain subdued, rising just 1 percent to 13.4 million hectares. Tight corn supplies should also encourage switching from soybeans in southern Brazil. Parts of Brazil coped with very dry conditions during this year's growing season, so with better weather assumed for next year, soybean output should rise modestly to 32.8 million tons from this year's 31.4 million. Slack world import demand may trim Brazil's soybean exports to 9.4 million tons in 2000/01 from 10.2 million.

China's Imports of Soybeans to Decline in 2000/01



2000/01 forecast.

Economic Research Service, USDA

A record *Argentine* soybean area is projected next year, a result mostly of expanded double cropping with wheat and some switching from sunflowers. A higher proportion of double-cropped soybeans would hold down the national average yield, however. Consequently, Argentina's soybean production is expected to rise only modestly from 20.7 million tons this year to 21.5 million in 2000/01. Larger competitor supplies and smaller world imports will limit Argentine soybean exports next year to 4.1 million tons, compared with 5.1 million this year.

China's Accession to WTO to Boost Soybean Product Imports

The future of Chinese agriculture, as well as world trade, will likely be transformed once the country gains admission to the World Trade Organization (WTO). As a prelude to getting consent from all WTO member countries, China has signed a bilateral agreement with the U.S.

The agreement would expand market access for soybean oil by replacing China's arbitrary, unannounced absolute quotas with a tariff-rate quota (TRQ). Under a TRQ, a lower tariff is applied to imports within the quota, while above the quota, no quantitative restriction exists provided the importer pays the higher, over-quota tariff. In principle, a country could set an over-quota tariff so high as to practically prohibit imports beyond the quota.

Under the bilateral agreement, the quantity of soybean oil that China would allow under the TRQ increases from 1.72 million metric tons next year to 3.26 million by 2006. The within-quota duty would be 9 percent (compared with 13 percent currently), and the over-quota duty would gradually decline from 74 percent to 9 percent by 2005. This reduction effectively eliminates the TRQ, leaving just a low 9-percent tariff (equivalent to rates in other WTO countries) on an unlimited volume of soybean oil imports.

An increasing proportion of the quota, which is now only available to a few state-owned importers, would be allocated to nonstate traders. China's tariff on soybeans (3 percent) and soybean meal (5

percent) would be bound at their current low rates. Subsidized agricultural exports would be forbidden.

Soybean oil exports from the U.S. (as well as from Argentina and Brazil) will almost certainly expand as China's over-quota tariff declines over the next 3 to 4 years, although the tariff-rate quota might not be entirely filled immediately after implementation, depending on China's vegetable oil consumption and domestic production. Competition in China's vegetable oil market will also arise from accession agreements between China and other countries, which increase import access for canola oil and palm oil.

Reducing China's import barriers on vegetable oil could sharply increase oil imports and drive down internal prices. Since many Chinese crushing facilities are much less efficient than Western plants, the reduction in processing margins should reverse the recent expansion in oilseed crushing and revive imports of soybean meal as well.

Because of its size, China is already one of the world's largest consumers of soybean meal and soybean oil. However, China's per capita use is still relatively low compared with developed nations, and lower prices could stimulate consumption. Following WTO accession, initial USDA estimates (*AO* March 2000) of the average change in value over baseline projections of China's imports during the next decade are: soybean oil, $352 million higher; soybean meal, $220 million higher; and soybeans, $402 million lower.

With concurrent changes in China's grain and livestock sectors, it is uncertain what would be the net effect on China's domestic oilseed production, as policies in previous years have generally been skewed toward grain production. Allowing more meat imports into China will also affect domestic feed consumption. Without domestic subsidies, it is likely that Chinese oilseed farmers will switch to more profitable crops or quit agriculture as they are exposed to more competition from more efficient foreign producers.

The rest of the world's oilseed crushers welcome lower protection for China's farmers and domestic processors, and greater opportunities to export oilseed products. Both the U.S. and Argentina substantially expanded crushing capacity in the 1990's. As China's policies promoted domestic oilseed crushing, considerable excess capacity developed, and crush margins throughout the world sharply narrowed. China's soybean crushing increased by nearly one-fourth in 1999/2000, while world crush (excluding China) declined 1 percent. The supply gluts have been most acute in the global vegetable oil market, as robust gains in palm oil output further depressed prices.

Price Competition To Remain Keen

Competitive prices are seen securing solid growth in U.S. soybean product demand, after 2 years of poor margins and declining crush rates. Domestic demand for both soybean meal and oil is expected to grow modestly in 2000/01, generally exceeding gains in export demand. U.S. soybean crush is expected to rise to 1.625 billion bushels in 2000/01 from 1.57 billion last season.

Low feed costs and rebounding prices in the hog sector should begin to promote herd expansion again next year. Domestic disappearance of soybean meal is projected up 3 percent to 31.25 million short tons, compared with an estimated 1-percent decline in 1999/2000. Soybean meal prices are forecast at $140-$165 per short ton vs. $165 last season.

With abundant U.S. and foreign soybean and soybean oil supplies, price competition will be keen. Projected U.S. soybean oil prices for 2000/01 are 15-18 cents per pound, little changed from the 1999/2000 average of 15.7 cents. Competitive prices and targeted foreign food aid will better position U.S. soybean oil exporters next year, and comparatively weak 1999/2000 export shipments of 1.2 billion pounds are forecast to recover to 1.8 billion next season. Domestic disappearance of soybean oil is anticipated up nearly 3 percent to 16.65 billion pounds.

Like their U.S. counterparts, South American oilseed processors have seen poor margins that prevented them from operating at full capacity. In Argentina, domestic soybean crushing is likely to remain stagnant in 2000/01, edging up just 0.1 million tons from 16.9 million in 1999/2000. In Brazil, slightly larger domestic supplies and stronger export and domestic demand for soybean meal and oil are boosting crush from 21.1 million tons in 1999/2000 to 21.6 million. Brazilian soybean meal exports, particularly to Europe, have benefited from the country's depreciated exchange rate. Competition from Brazil sharply curtailed U.S. soybean meal exports to Europe in 1999/2000.

Brazil's crushers (located mostly in the south) will need larger supplies to remain competitive. Access to soybeans grown in the expansion areas of the center-west has been complicated by interstate value-added taxes, which make it more profitable to export soybeans than to crush them domestically.

Despite anticipated trade liberalization, substantial growth in China's imports of soybean products is not expected in the near term. Therefore, the strength of Chinese import demand for soybeans will be a key determinant in the consumption of U.S. and South American crops in 2000/01. But given an already huge expansion in the U.S. harvest, an increase in world soybean prices remains unlikely, even in the most optimistic analysis of Chinese and EU demand. AO

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